CORDA

TOGETHER WE'RE INVESTED

Value Versus Growth

There is a quote from Benjamin Graham, the father of value investing, that comes to mind when considering the price action of the stock market. He said; "Basically, price fluctuations have only one significant meaning for the true investor. They provide him with an opportunity to buy wisely when prices fall sharply and to sell wisely when they advance a great deal. At other times he will do better if he forgets about the stock market and pays attention to his dividend returns and to the operating results of his companies."

2015 was a case study exactly to that regard. The Dow Jones Industrial average and the S&P 500 Index both finished the year about where they first started. The path along the way, 252 trading days in all, was far from a stalemate. The market had a couple of bouts of panic, especially on the morning of August 24th when the Dow opened down more than 1,000 points, and for many investors, the whole year was extremely difficult to sustain with patience and equanimity. We have learned through years of experience and study that the successful investor will use the price action to their advantage and will seek opportunities where others see misfortune.

Life lessons and analogies to the stock market can be viewed through the lens of a meteorologist. What might the following series of numbers represent? 643, 680, 656, 654, 667, 626, 631, 628, 623, and 675? I'm sure the last thing you expected from your portfolio management team at CORDA was to open the year with a quiz, right?! Well, we couldn't resist.

Those numbers are the last ten years' readings taken from the Lower Colorado River Authority for Lake Travis' month end December water level measured in feet. Lake Travis is a delightful man-made lake on the outskirts of Austin, Texas. Many parts of Texas, much like southern California, have been under extreme drought conditions for many years. In 2006, the lake was at 643 feet, and a year later at the end of 2007, it was up to 680 feet (which incidentally is considered a full water table for this particular lake in central Texas). However, over the subsequent seven years, the lake dwindled to the 623 foot level recorded about this time last year. Then, as many of you know, starting this past spring, Texas has received an inordinate amount of rain and storms and other vibrant weather conditions, up to and including some tragic and violent storms in the Dallas/Ft. Worth area right after the Christmas holiday.

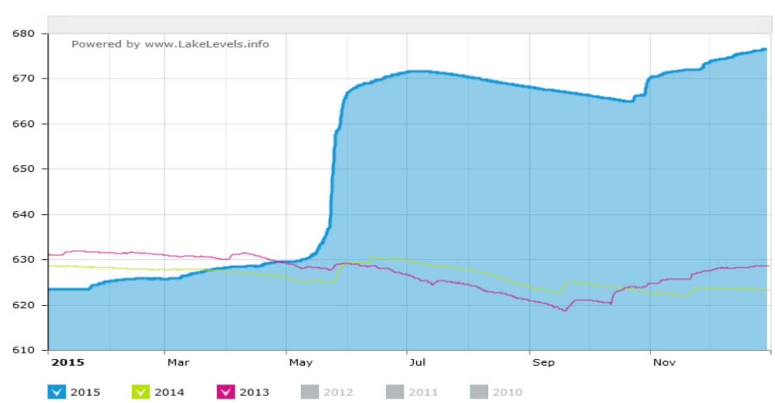
The point being, predicting weather conditions, rain storms, and other events like droughts is plainly difficult. So, too, is attempting to predict or time the market. Since one cannot accurately predict when a single company will appreciate in value, building a diversified portfolio of companies with most paying attractive dividends will typically lead to a successful result. One must be willing to hold the investment a suitable period of time unless something fundamental has changed.

We have been finding a host of attractive investment opportunities with attractive dividends and/or dividend growth potential that have traded down for one reason or another. In addition, we believe they can be purchased at attractive valuations and have appealing metrics across the board and appear to offer long term total return potential. That said, some of the laggards by way of short term price action in our portfolio can be seen as offering just as much if not more upside in the coming years if the shares return to what we consider fair value.

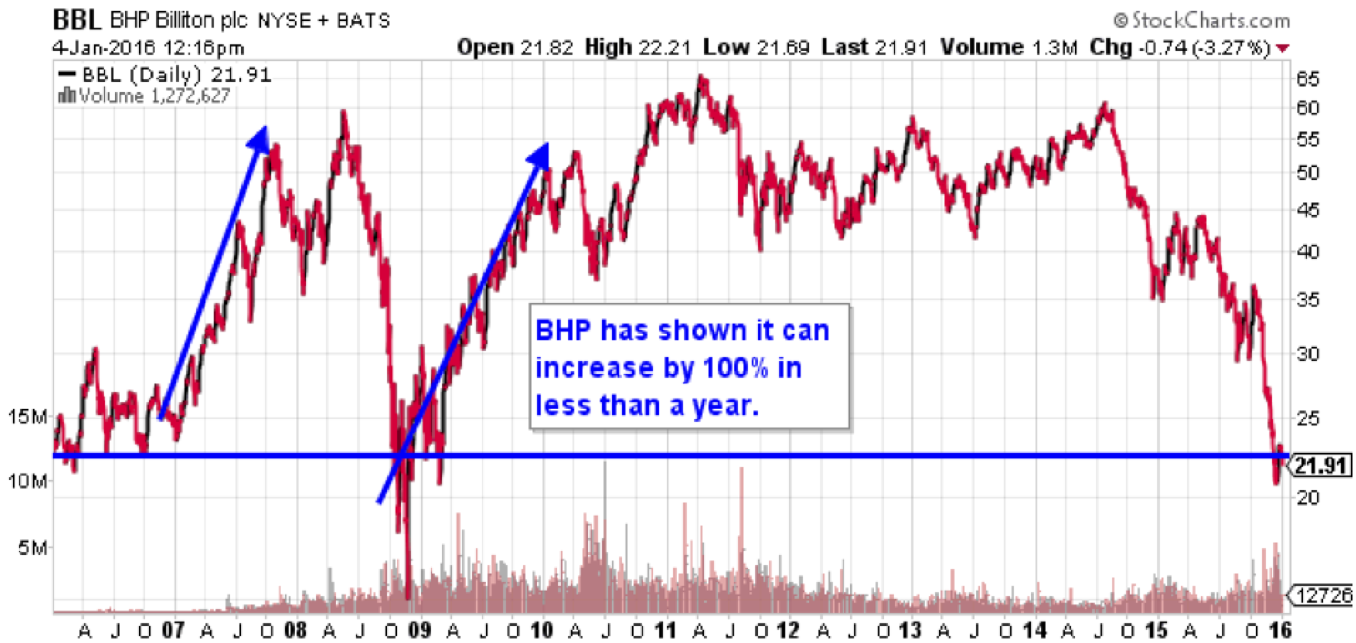
We consider ourselves to be well positioned as we usher in a new year. The ebb and flow of the economy, central bank decisions, political policy changes – are a constant. There will always be something to fret about. However, protecting and growing your wealth over time is what we will stay unilaterally focused on in 2016 and beyond.

As a reminder, our philosophy through almost every market condition is to rely on large, reliable, and growing dividends paid out from healthy, sound, and competitively advantaged businesses. We find this is the surest way to long term success via total returns from dividends and appreciation. Our principles are timeless, yet sometimes we must wait for longer time periods than anticipated! We will continue to focus on identifying and owning the highest quality companies. It is a natural process. We certainly haven't and likely won't ever attempt to time the overall market, but we will maintain a strict focus on owning quality businesses at good value. Those with high quality have characteristics of strong dividends, a sound balance sheet, predictable revenues and earnings, and a penchant for rewarding shareholders through dividend hikes and/or share buybacks over time. We will maintain our penchant for the value approach and it will serve our needs well as global economies, interest rates, and political forces cause markets to fluctuate on a daily basis.

Keep in mind, markets can change suddenly and without warning. The ever changing weather pattern is a reminder to this. Today, we are told meteorologists are forecasting significant rain in southern California for later this week, and the massive floods in the Midwest are a testament to how quickly things can change. This is especially true of the stock market. Pundits and talking heads will seek to entertain you on a daily basis, and it will be our job to keep you focused on the big picture. The graph below shows how quickly Lake Travis recovered in 2015!



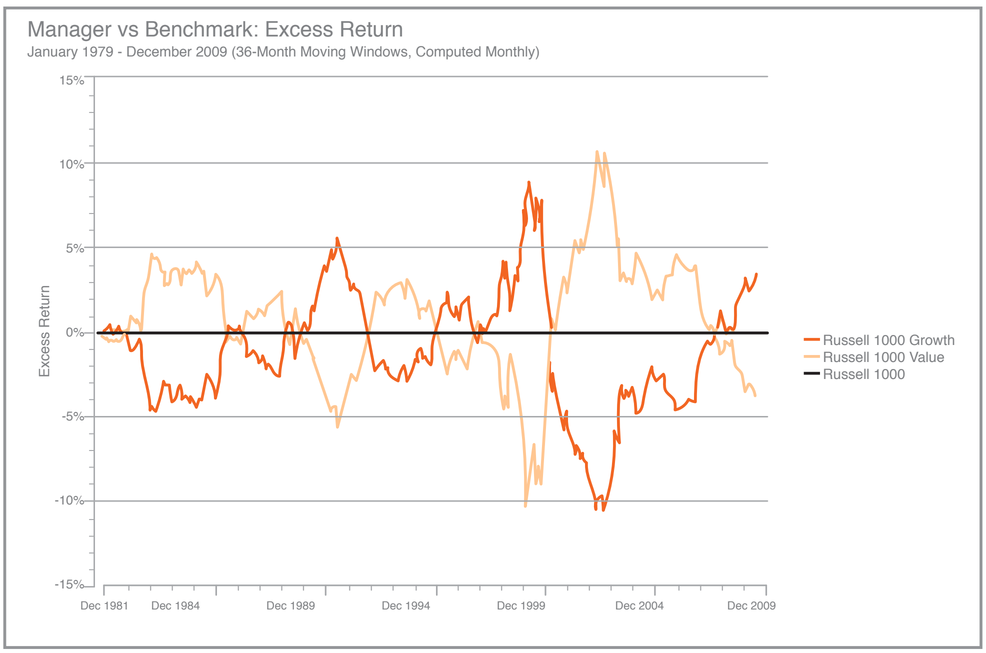
If the water table of Lake Travis can recover, is it possible the stock price of a large global multi-national business can recover as well? Here's a ten year chart of BHP Billiton:



Additional data points for you to ponder as we head into 2016:

Growth stocks have been outperforming value for a couple of years now. CNBC likes to talk about the FANG's – Facebook, Amazon, Netflix and Google (now Alphabet). These four businesses can be categorized as growth companies – typically classified as growth are those that do not pay dividends, many times do not make profits or reinvest all earnings back into the business, or trade at higher valuations…without these four last year, the S&P 500 would have been down ~5% instead of essentially unchanged. That's a huge impact from just four companies.

The key takeaway is that growth does not always outperform. We own tried and true value businesses because we seek dividend income, more predictability, diversity and stability. The chart below is a comparison of the growth part of the market versus the value part over the past two years. Growth shares have out-performed value by a whopping 51.5%. This cannot sustain itself. The second chart depicts the relationship between value and growth for the thirty year period between 1979 and 2009. It is compelling that there are periods when one or the other is out performing, but clearly not the case that growth always wins out. The time to buy value is when the divergence is large. We are in that zone right now. Therefore, owning the value segment is where you want to be invested right now.



Bottom line, in contrast to the market value of our portfolio, which we cannot predict or control, what we can do is anticipate and influence the growth of our income. If we succeed in increasing our annualized income at a good pace over time, it's reasonable to expect the market value of our portfolio to trend upward as well.

We are delighted to enter a new year with you and we wish that 2016 will be a pleasant year for you and your loved ones.

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John Schloegel

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